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No. 82-6

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

LLOYD KYPTA,

Petitioner,

v.

McDONALD'S CORPORATION, McDONALD'S SYSTEM, INC., and FRANCHISE REALTY INTERSTATE CORPORATION,

Respondents.

On Petition for Writ of Certiorari to the Court of Appeals for the Eleventh Circuit

BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

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QUESTION PRESENTED

Whether the Court below—on the basis of the specific facts of the case and, in particular, petitioner's admissions and deficiencies of proof—correctly held that petitioner failed to meet his burden of showing an actual injury as required by § 4 of the Clayton Act.

TABLE OF CONTENTS

	PAGE
Question Presented	i
Table of Authorities	iii
Statement of the Case	1
A. McDonald's Business And Its Franchising Method	1
B. The 79th Street Restaurant	3
C. The Proceedings Below	5
Reasons Why The Writ Should Be Denied	7
I. Contrary To Petitioner's Statement Of The "Question Presented For Review", The Decision Below Does Not Present Any Issue As To Elements Of A Tie-In Violation Or The *Per Se* Standard	8
II. The Decision Below Concerns Only Petitioner's Failure To Prove Any Actual Injury	9
III. There Is No Conflict	11
Conclusion	14

TABLE OF AUTHORITIES

Cases

	PAGE
Bigelow v. RKO Pictures, Inc., 327 U.S. 251 (1946) ..	9
Bogosian v. Gulf Oil Corp., 561 F.2d 434 (3d Cir.), *cert. denied*, 434 U.S. 1086 (1977)	11
Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477 (1977)	9
Flintkote Co. v. Lysfjord, 246 F.2d 382 (9th Cir.), *cert. denied*, 355 U.S. 835 (1957)	9
Gray v. Shell Oil Co., 469 F.2d 742 (9th Cir. 1972), *cert. denied*, 412 U.S. 943 (1973)	9
Hawaii v. Standard Oil Co., 405 U.S. 251 (1972)	9
J. Truett Payne Co. v. Chrysler Motors Corp., 451 U.S. 557 (1981)	9
Kestenbaum v. Falstaff Brewing Corp., 514 F.2d 690 (5th Cir. 1975), *cert. denied*, 424 U.S. 943 (1976) ...	9
Krehl v. Baskins-Robbins Ice Cream Co., 78 F.R.D. 108 (C.D. Cal. 1978)	11, 12
Kypta v. McDonald's Corp., 1980-1 Trade Cases ¶ 63,267 (S.D. Fla.)	6
Malcolm v. Marathon Oil Co., 642 F.2d 845 (5th Cir.), *cert. denied*, 102 S.Ct. 975 (1981)	12
Northern Pacific Ry. Co. v. United States, 356 U.S. 1 (1958)	11
Principe v. McDonald's Corp., 631 F.2d 303 (4th Cir. 1980), *cert. denied*, 451 U.S. 970 (1981)	3
Siegel v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir. 1971), *cert. denied*, 405 U.S. 955 (1972)	12, 13
State of Alabama v. Blue Bird Body Co., 573 F.2d 309 (5th Cir. 1978)	9

PAGE

United States Steel Corp. v. Fortner Enterprises, Inc., 429 U.S. 610 (1977) 13

Statutes

15 U.S.C. § 1 5

15 U.S.C. § 15 5

United States Supreme Court Rule 17 8

Other Authorities

Areeda, Antitrust Violations Without Damage Recoveries, 89 Harv. L. Rev. 1127 (1976) 13, 14

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STATEMENT OF THE CASE

A. McDonald's Business And Its Franchising Method.

McDonald's is the owner of "McDonald's" fast-service, limited-menu restaurants which McDonald's has located and developed throughout the country.

In each restaurant it develops (including each restaurant it franchises), McDonald's itself invests a very substantial sum (in 1980 averaging over $530,000 per unit) for the site itself and the restaurant building constructed on it (the amount in each instance depending on location and type of

building). Approximately one-quarter of McDonald's restaurants are company-operated; the remainder are operated by franchisees.

As the parties stipulated (Turner Dep. pp. 7-9, 127-28), and as the District Court found (App.[1] 26), McDonald's does not engage in "rent-a-name" franchising (in which the franchisor merely authorizes the use of its name and concepts in the franchisee's own stores or restaurants). Instead, a McDonald's franchise consists of the rights and authorizations essential to enable the franchisee to operate for an agreed term (usually 20 years) a specific McDonald's restaurant located, developed and owned by McDonald's.

Also unlike many "rent-a-name" franchisors, McDonald's does not sell any foodstuffs, supplies or other common articles to its franchisees. (Coons Dep. p. 23.) Instead, apart from the initial payments from the franchisee (generally a $12,500 franchise fee and a refundable $15,000 security deposit), McDonald's sole source of franchising income consists of monthly payments received from its franchisees based on the sales (currently 11½%) of its franchised restaurants. (*Id.* at 26.)

After it is decided to build a McDonald's restaurant on a particular site, a separate and independent decision is made as to whether the restaurant should be company-operated or whether it should be franchised. If the decision is to franchise the store, McDonald's begins the process of locating a franchisee, which involves offering the store either to an existing franchisee or to an applicant on the franchise waiting list.

As already noted, in each restaurant it franchises, McDonald's itself invests a substantial sum. Consequently, it has been possible for McDonald's franchisees (including petitioner Kypta) to become a McDonald's operator with

[1] "App." refers to the appendix of record excerpts included in petitioner's brief in the Court of Appeals. "Pet. App." refers to the appendix to the petition for certiorari.

a much smaller investment than the total investment required for restaurant ownership. In addition, since McDonald's owns the restaurant and is entitled to regain possession at the end of the term or in the event of a default, it is able to maintain a location as part of its restaurant system, irrespective of the success or failure of any individual operator.[2]

McDonald's investment in real estate is solely a function of its ownership of the McDonald's restaurants which it locates and develops.

B. The 79th Street Restaurant.

It was within this framework that petitioner obtained operating rights to the McDonald's restaurant at 3325 N.W. 79th Street in Miami.

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[2] McDonald's franchising method was recently explained in greater detail by the Court of Appeals for the Fourth Circuit in *Principe* v. *McDonald's Corp.*, 631 F.2d 303 (4th Cir. 1980), cert. denied, 451 U.S. 970 (1981). *Principe* involved the identical "real estate tie-in" claim; in addition, counsel for petitioner in this case represented the plaintiff in *Principe*. In the course of its decision rejecting the tie-in claim on the merits (for lack of two separate tying and tied products), the Fourth Circuit pointed out that McDonald's franchising method has resulted in "substantial advantages, both for the company and for franchisees." (631 F.2d at 309-10.) Thus, McDonald's franchising method (a) enables McDonald's "to obtain better sites than franchisees could select" (*id.* at 310); (b) "assures that the [franchised] stores remain part of the McDonald's system" regardless of the success or failure of an individual operator, thereby "preserving the goodwill of the system in established markets" (*ibid.*); (c) "reduces a franchisee's initial investment, thereby broadening the applicant base and opening the door to persons who otherwise could not afford a McDonald's franchise" (*ibid.*); and (d) contributes to the creation of a beneficial community of interest between franchisor and franchisee since "both McDonald's and the franchisee have a substantial financial stake in the success of the restaurant . . ." (*ibid.*).

In April 1965, nearly a year before Kypta was even considered for a franchise at that location, McDonald's purchased the vacant 79th Street lot for $41,325. In December 1965, McDonald's entered into a contract for the construction of the restaurant building for the additional cost of $74,659. (Defendants' Answers to Plaintiff's Sixth Set of Interrogatories, Answer to Interrogatory No. 3, R. 1701.)

When Kypta first contacted McDonald's about the possibility of obtaining a McDonald's franchise, he worked for the United States General Accounting Office in St. Louis, Missouri, and had a yearly income of $14,595 (Kypta Dep. pp. 417-18). Kypta's only experience in the restaurant business was volunteer work for a McDonald's franchise in St. Louis "just to learn the business" (*id.* at 6).

Kypta went to Chicago and met with a McDonald's representative to discuss possible franchise locations (*ibid.*). Although Kypta preferred the St. Louis area, he was willing to "take a unit anywhere where it was good . . . I was looking for a good location primarily" and asked McDonald's to offer various locations to him so that he could determine whether or not they would be good (Kypta Dep. p. 8). Kypta expected, as a result of his meeting at McDonald's, that McDonald's would continue to offer him locations until a location which he found suitable became available (*id.* at 17).

In fact, McDonald's did offer Kypta several locations in Kansas, California, Louisiana, Virginia and Florida. Kypta inspected some of these sites before rejecting them; he rejected other sites without examining the location. (*Id.* at 8-17.) Finally, in March 1966, although Kypta had originally rejected the 79th Street location after inspecting it (following commencement of construction of the restaurant), he accepted McDonald's offer of a franchise to operate the restaurant at that location (*id.* at 18).

McDonald's franchise offer called for an initial franchise payment of $27,500 (including a refundable $15,000 security deposit) plus monthly payments calculated on the basis of 9.2% of sales for the rights to operate the restaurant for a 20-year term. These operating rights and corresponding obligations were subsequently detailed in two interrelated documents prepared, presented and executed at the same time—a lease authorizing occupancy of the 79th Street restaurant (and providing for payment of 7% of sales against a monthly fixed-dollar minimum); and a license authorizing use of McDonald's name and trademarks at the 79th Street restaurant (and providing for payment of 2.2% of sales).

C. The Proceedings Below.

In April 1973, after operating the 79th Street restaurant for nearly seven years under the franchise, and following McDonald's refusal to grant him a second such franchise at another location (Kypta Dep. pp. 26, 32), petitioner Kypta brought this action under § 4 of the Clayton Act (15 U.S.C. § 15) charging that the franchise for the 79th Street restaurant violated § 1 of the Sherman Act (15 U.S.C. § 1). In his complaint Kypta alleged *inter alia* that McDonald's had unlawfully "tied" the license and lease contracts relating to the 79th Street restaurant.

Kypta testified on deposition that he knew of no facts which would demonstrate that he would have been financially better off had he owned his own restaurant and obtained only the right to use McDonald's name. Kypta also admitted that he had no basis for believing that he would have been able to negotiate a better lease agreement with another lessor, or that the fees paid to McDonald's would have remained the same if McDonald's merely granted

Kypta the right to use McDonald's name in a restaurant owned by Kypta. (Kypta Dep. pp. 432-33, 444.)[3]

On the basis of Kypta's admissions and stipulations, McDonald's moved for summary judgment on the "real estate tie-in" claim. While denying that Kypta could meet any of the requirements for proving an illegal tying arrangement, McDonald's contended that Kypta could not in any event prove the requisite injury or "fact of damage". In particular, McDonald's contended that Kypta could not prove that he could have obtained at less cost an alternative location of comparable value. In his written response to the motion and at the hearing held on the motion, plaintiff acknowledged that he could not and would not offer such proof if a trial were held, but contended that such proof was unnecessary as a matter of law.

After analysis of the parties' positions, and relying on Kypta's admissions and stipulations, the District Court granted the motion for summary judgment (1980-1 Trade Cases ¶ 63,267). The Court concluded (see Pet. App. 5):

> "If there were an antitrust violation, which this Court seriously doubts, Plaintiff simply is not in a position to show fact of damage. A trial on the issue before the Court would serve no useful purpose."

On appeal, the Court below unanimously affirmed. The Court held (Pet. App. 10-11):

> "Because the location of a restaurant is crucial to the volume of sales, Kypta's inability to offer evidence of a specific alternate location and projected

[3] In addition, Kypta admitted that he had no factual basis for believing that he could have afforded to become the owner of a McDonald's restaurant building at the time he first became a McDonald's franchisee or that he would have been able to arrange a conventional mortgage for the purchase of the restaurant building and property. (Kypta Dep. p. 423.)

profitability there renders his claim of economic injury bogus.

• • •

"While there is no dispute between the parties regarding the cost of the tied product, the appellant has not even attempted to introduce evidence regarding its actual value. . . .

• • •

"Kypta acknowledges that he can neither show a different location equally as profitable as that of his present restaurant nor demonstrate that he was charged more than the reasonable value of his lease and license. These concessions render blows fatal to his appeal."[4]

Accordingly, the Court concluded (Pet. App. 13) that ". . . trial would serve no useful purpose, in view of the plaintiff's admitted inability to satisfy one basic element of his claim—that of economic injury. . . ."

REASONS WHY THE WRIT SHOULD BE DENIED

As examination of the decision below readily confirms, the decision is based on the specific facts of this case and, in particular, on petitioner's admissions and deficiencies of proof.

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[4] With respect to Kypta's alternative argument based on the refundable security deposit paid to McDonald's, the Court held (Pet. App. 12):

"The appellant does not challenge here the trial court's grant of summary judgment as to the security deposit tie-in claim; he does contend that the security deposit is an element of his claimed damage as to the real estate tie-in charge. Yet, the plaintiff's allegation that his loss of use of that $15,000.00 since 1966 represents injury regardless of whether there was an overcharge on the lease is untenable. Kypta fails to show that this part of the overall package caused him *net* economic damage which, as we observed above, is the standard by which the *fact* of damage is determined." (Italics the Court's.)

None of the relevant considerations governing review on certiorari, as set forth in this Court's Rule 17, supports the grant of the requested writ. The decision of the Court of Appeals is wholly consistent—and is not in conflict—with the decisions of this Court and the other Courts of Appeals. Nor does the decision below merit review by this Court for any other reason.

I. Contrary To Petitioner's Statement Of The "Question Presented For Review", The Decision Below Does Not Present Any Issue As To Elements Of A Tie-In Violation Or The *Per Se* Standard.

In what can only be regarded as a flagrant distortion, petitioner asserts that the "Question Presented for Review" involves "creation by a federal appeals court of a test which pragmatically eliminates tying as a per se violation" (Pet. p. i). With similar abandon, petitioner asserts that the impact of the decision below is ". . . to replace the old *per se* standard with a new rule of reason standard in all tying claims. . . ." (Pet. p. 8.)

Petitioner's assertions are frivolous. As petitioner inconsistently acknowledges elsewhere in the petition, neither the District Court nor the Court of Appeals even passed on the violation question or the standard for establishing a tie-in—*per se*, rule of reason, or any other test. Thus, petitioner states quite correctly (Pet. p. 4):

> "The trial court decided that Kypta could not prove that he had been injured—i.e., fact of damage—and summarily adjudicated Kypta's claims in favor of McDonald's. Expressed as dictum was the district court's belief that no violation has been established; *the decision did not however turn on proof of violation.* The amount of damage issue was not reached, because proof of any injury at all was found lacking.
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> • • •
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> "The court of appeals *carefully avoided deciding whether a violation had been established, but affirmed*

the prior decision on the fact of damage issue." (Italics added.)

II. The Decision Below Concerns Only Petitioner's Failure To Prove Any Actual Injury.

That question—"the fact of damage issue"—is of threshold importance in a private antitrust action under § 4 of the Clayton Act. It is well-settled that the gravamen of such an action is not the violation but is instead the plaintiff's injury. And such injury, as this Court recently reemphasized,[5] must be *actual*—not theoretical or hypothetical or "automatic". It was solely on that basis that the courts below rejected petitioner's claim.

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[5] *J. Truett Payne Co.* v. *Chrysler Motors Corp.*, 451 U.S. 557, 562 (1981) (". . . proof of a violation does not mean that a disfavored purchaser has been actually 'injured' within the meaning of § 4"). See also *Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 486 (1977) (injury must be "actually proved"; proof of a violation "establishes only that injury may result"); *Hawaii* v. *Standard Oil Co.*, 405 U.S. 251, 262 (1972) ("three times their actual damages"). Furthermore, ". . . the jury may not render a verdict based on speculation or guesswork". *Bigelow* v. *RKO Pictures, Inc.*, 327 U.S. 251, 264 (1946). Accord, e.g., *Gray* v. *Shell Oil Co.*, 469 F.2d 742, 749 (9th Cir. 1972), cert. denied, 412 U.S. 943 (1973) (" 'By its own terms, Clayton Act recovery is available only where actual injury has been suffered' "); *Kestenbaum* v. *Falstaff Brewing Corp.*, 514 F.2d 690, 695 (5th Cir. 1975), cert. denied, 424 U.S. 943 (1976) (plaintiff has "burden of establishing a net economic loss").

In addition, in contrast with proof of the *amount* of damages, injury—the *fact* of damage—must be clearly established. See, e.g., *State of Alabama* v. *Blue Bird Body Co.*, 573 F.2d 309, 317 (5th Cir. 1978); *Flintkote Co.* v. *Lysfjord*, 246 F.2d 386, 392 (9th Cir.), cert. denied, 355 U.S. 835 (1957) ("the burden as to [fact of damage] is the more stringent one" and "must first be shown before the jury is allowed to estimate the amount of damage").

Furthermore, it is clear that the decisions below turned on the specific facts of this case. Even more significantly, the decisions below rest on this particular plaintiff's admissions and failures of proof. This is acknowledged by petitioner, who states that "The decision of the court of appeals turned specifically upon what it found to be three failures of proof by Kypta. . . ." (Pet. p. 5.)

Thus, petitioner admitted below—and repeats in this Court—that "He did not show that he could have afforded and found a suitable alternate location which would have been as profitable as the one McDonald's required him to lease" (*ibid.*). Indeed, petitioner now states that "He therefore has absolutely no idea, nor does anyone else, what he *might have* been able to acquire by purchase or lease, nor has he the least idea what would have been the profits of that non-existent restaurant located at some hypothetical, alternate location." (Pet. p. 23, italics petitioner's.)

Petitioner claims he was overcharged for the alleged tied product and acknowledges the need to ". . . determine whether he paid more for the use of the restaurant premises than he would have, absent a tie. . . ." (Pet. p. 23.) But petitioner offered no proof as to what an alternative location of comparable value would have cost him. Without that elementary calculation—which petitioner states he cannot make—there is not the slightest basis for determining that he was overcharged and thereby actually injured under any standard.

Instead of showing that he paid more than the fair value of the premises, petitioner relies on the fact that he paid more "rent" to McDonald's than the amount which McDonald's paid for the real estate which he leased from McDonald's—in short, that McDonald's made a profit. But McDonald's cost for that particular site does not remotely show that petitioner could have obtained an equally profitable site at another location for the same amount. As the Court below noted, ". . . the location of a restaurant is

crucial to the volume of sales. . . ." (Pet. App. 10),[6] and the possible availability of some other site at a lower rent but of less profitability is wholly insufficient to show any actual injury.

Thus, even apart from petitioner's failure to prove the fair value of the alleged tying product (and even assuming *arguendo* that petitioner had the financial resources to build a restaurant at an alternative site and that he was able to induce the owner of that site to sell or lease it to him[7]), petitioner's failure to prove the fair value of a comparable alternative to the alleged tied product precludes any recovery.

III. There Is No Conflict.

The decision below is not in conflict with any decision of this Court or any other Court of Appeals.

As already pointed out, the decision below does not even pass on any of the substantive elements of a tie-in. And, on the fact of damage issue, the decision merely applies, to the specific facts of this case, this Court's decisions that a treble-

[6] Indeed, every site is inherently unique; real estate (unlike, e.g., standardized equipment) is not fungible. See *Northern Pacific Ry. Co.* v. *United States*, 356 U.S. 1, 7 (1958); *Bogosian* v. *Gulf Oil Corp.*, 561 F.2d 434, 453-54 (3d Cir.), cert. denied, 434 U.S. 1086 (1977).

[7] In many instances, McDonald's involvement in the process of restaurant development and leasing is not merely a matter of the operator's choice and McDonald's wishes, but is also the result of the landowner's demands as well. Although a prospective franchisee may desire to lease a specific site, the landlord may be unwilling to enter into a 20-year lease with an unknown individual. The landlord may be quite willing, however, to deal with a nationally-known corporation like McDonald's. "The size and reputation of a tenant is a vitally important factor in determining the terms of a commercial lease." *Krehl* v. *Baskins-Robbins Ice Cream Co.*, 78 F.R.D. 108, 121 (C.D. Cal. 1978).

damage plaintiff must prove actual injury and is not entitled to "automatic damages".[8]

Equally without merit is petitioner's suggestion of a conflict with the Ninth Circuit's decision in *Siegel* v. *Chicken Delight, Inc.*, 448 F.2d 43 (9th Cir. 1971), cert. denied, 405 U.S. 955 (1972). On the contrary, the Court below expressly relied on *Siegel* in holding that petitioner had not only failed to prove the value of the alleged tied product (the lease) but also had failed to take into account the value of the alleged tying product (the license).

In *Siegel*, contrary to petitioner's contention, the Ninth Circuit held that the value of *both* products must be compared with total payments (448 F.2d at 52):

> "The question here is whether the plaintiffs have suffered injury by virtue of the unlawful arrangement to which they were subjected. That arrangement of necessity involved *both tying and tied products.* To ascertain whether an unlawful arrangement for the sale of products has caused injury to the purchaser, the cost or value of the *products* involved, free from the unlawful arrangement, must first be ascertained." (Citation omitted, italics added.)

See also *Krehl* v. *Baskin-Robbins Ice Cream Co.*, 78 F.R.D. 108, 121 (C.D. Cal. 1978).[9]

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[8] *Malcolm* v. *Marathon Oil Co.*, 642 F.2d 845 (5th Cir.), cert. denied, 102 S.Ct. 975 (1981), discussed at Pet. pp. 18-20, is not to the contrary. *Malcolm* recognizes that plaintiff must introduce "substantial evidence of injury caused by the alleged violations and the amount of damages." (642 F.2d at 852.) The law review article quoted at Pet. pp. 18-19 is precisely to the same effect.

[9] While purporting to quote *Siegel* "in context", petitioner (Pet. pp. 16-17) seeks to skip over the Ninth Circuit's main holding on the damage issue and quotes instead another paragraph of the *Siegel* opinion where the Ninth Circuit rejected an *additional* argument never even made in this case—namely an argument "that since the value of the tying items must be taken into account, as a matter

That rationale is particularly appropriate where as here the alleged tying and tied products are "purchased" in a single transaction. Cf. *Principe* v. *McDonald's Corp.*, 631 F.2d 303 (4th Cir. 1980), cert. denied, 451 U.S. 970 (1981). The alleged tying product is a license to use (at the leased restaurant) McDonald's name and trademarks—a license which petitioner acknowledges is enormously valuable. He also admits that he has "no idea" what McDonald's would have charged for a license on a "rent-a-name" basis (Kypta Dep. p. 44). Furthermore, he does not challenge the fairness of the 9.2% for the package. Instead, his complaint is merely that the percentage assigned to the lease portion of the package is too high, regardless of the fairness of the overall percentage.[10]

As in *Fortner II*, if there be a tie-in, ". . . a higher price for the tied product is consistent with the possibility that the [alleged tying product] was unusually inexpensive and . . . the price for the entire package was equal to, or below a competitive price." *United States Steel Corp.* v. *Fortner Enterprises, Inc.*, 429 U.S. 610, 618 (1977). See Areeda,

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of law [the franchisees] have suffered no injury." (448 F.2d at 52.) In the instant case, no such conclusive presumption was sought or utilized, and the *Siegel* paragraph quoted by petitioner is wholly irrelevant to petitioner's claim that it need not prove an actual injury.

[10] It is also noteworthy that the "rent" paid to McDonald's is not merely a charge for the physical occupancy of the premises. Instead, the amount specified as "rent" in each lease or sublease is a percentage of gross sales (over a specified base minimum) and thus reflects the earning power of the premises as a McDonald's restaurant. The right to occupy and use a particular restaurant building on a particular parcel of land therefore cannot be considered in isolation from the total package of operating rights, services and assistance which each franchisee receives from McDonald's as part of his franchise to operate that restaurant.

Antitrust Violations Without Damage Recoveries, 89 Harv. L. Rev. 1127, 1138 (1976).[11]

CONCLUSION

For the foregoing reasons, the petition should be denied.

Respectfully submitted,

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[11] Furthermore, if McDonald's had been obliged to engage in "rent-a-name" franchising, and if petitioner did not have to pay McDonald's any rent, it certainly cannot be assumed that the financial arrangement between McDonald's and petitioner would have otherwise remained precisely the same. More specifically, it cannot be assumed that McDonald's only charge for a "rent-a-name" franchise would have been merely the 2.2% specified in petitioner's present license. Indeed, he testified—and his counsel stipulated—that they had "no idea" what McDonald's would have charged for a "rent-a-name" franchise (Kypta Dep. p. 44), and petitioner's counsel repeated the concession at the summary judgment hearing. Plainly the market value of any particular franchising transaction depends on what a willing buyer (the prospective franchisee) is willing to pay, and on what a willing seller (the franchisor) is willing to accept, for the opportunity to operate a franchise in a particular place at a particular time, in comparison to other alternatives available to both of them.